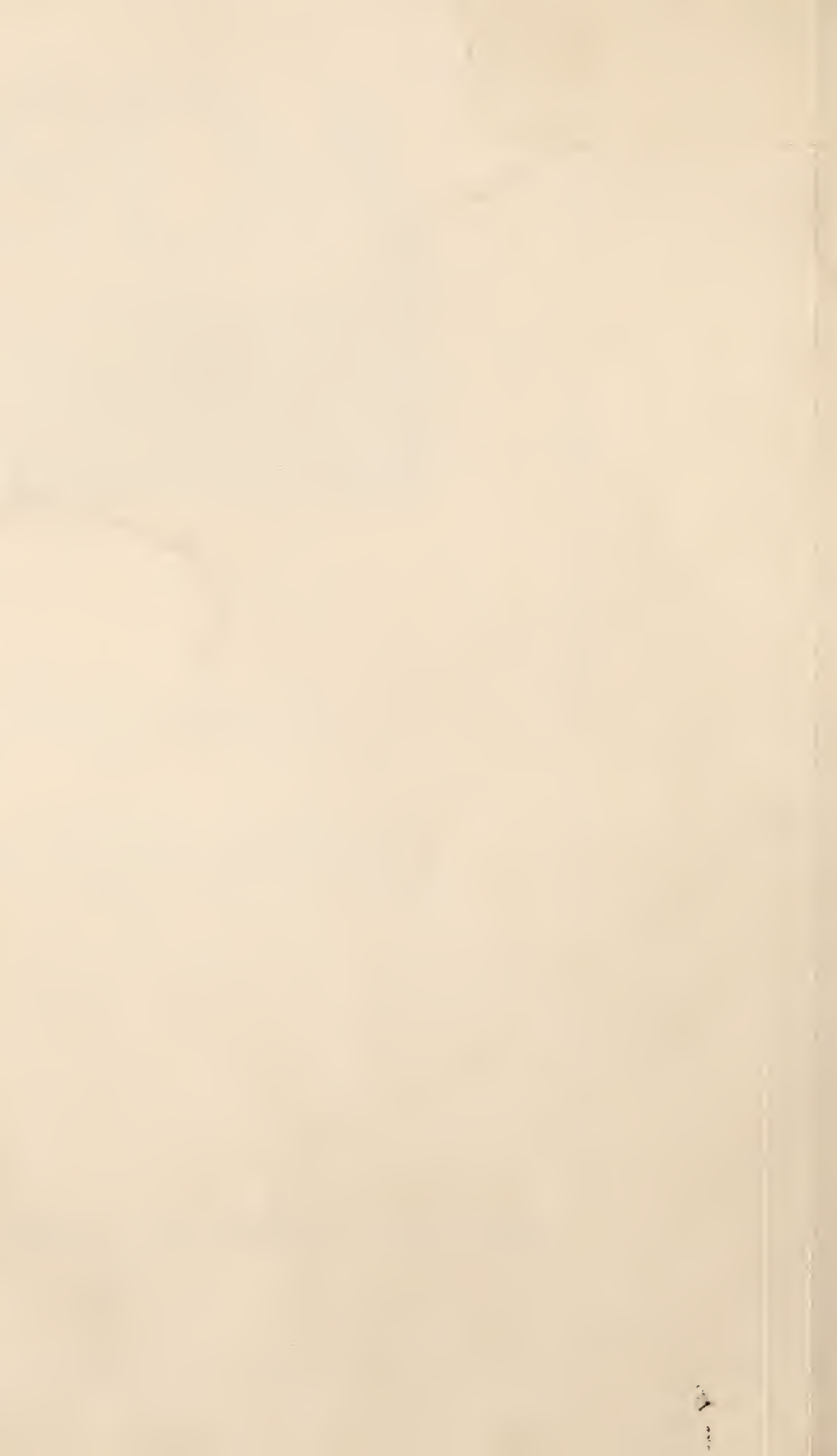


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United States  
Department of  
Agriculture

A 280.39 Agricultural  
AgSM Marketing  
Cop. 4 Bulletin  
Number 27

# The Federal Milk Marketing Order Program

JUL 17 '81

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## Preface

To work effectively, the Federal milk order program needs free, full and informed participation by all interested persons in the public proceedings which govern the orders. To that end, this publication is designed to provide a better understanding of the objectives of the program and the complex economic and marketing conditions of the dairy industry which provide the basis for Government involvement. It also explains the major provisions and the operation of the milk marketing orders.

*The Federal Milk Marketing Order Program*, Marketing Bulletin 27, was first published in October 1956 as Miscellaneous Publication No. 732, "Federal Milk Marketing Orders—Their Establishment, Terms and Operation." The first edition of Marketing Bulletin 27 was issued in July 1963 and revised in April 1968.

This edition revises sections on order provisions and administrative policy which have been changed since 1968 by marketing developments, new legislation and court decisions. *Questions and Answers on Federal Milk Marketing Orders*, AMS-559, provides a condensed version of this publication in question-and-answer form.

Revised June 1981



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### **The Federal Milk Marketing Order Program**

**by the  
Dairy Division  
Agricultural Marketing Service  
United States Department  
of Agriculture**

#### **Scope of the Milk Order Program**

During 1979, about 116,400 U.S. farmers delivered milk to handlers regulated by 47 Federal milk marketing orders. The value of the transactions was more than \$9.7 billion. About 85 percent of the farmers under the orders were members of dairy co-operative associations.

The marketing order areas include most of the Nation's major population centers; however, a number of milk orders have also been established for relatively small urban areas. In 1979, about 150 million Americans were consuming milk that had been processed by handlers under the Federal order program.

#### **Program Benefits**

Federal milk orders define the terms under which handlers of milk in a specified market purchase milk from dairy farmers. They are legal instruments designed to promote orderly marketing conditions by applying a uniform system of classified pricing throughout the market. Terms for the purchase of milk are spelled out in the order and are known in advance to both buyers and sellers, thus facilitating orderly marketing. Orders provide for the sharing among producers of the returns from all milk uses by requiring that payments for milk be pooled and that a uniform, or average, price be paid to individual dairy farmers or their cooperative associations.

Orders assist farmers in developing steady, dependable markets and help correct conditions of price instability and needless fluctuations in price. The dairy farmer is assured a minimum price for his milk which takes into consideration the economic conditions throughout the year. This high degree of assurance makes dairy farmers

willing to make the heavy investments in milk cows and equipment that are needed to produce high-quality milk.

Milk marketing orders also benefit handlers. They are assured that their competitors are not paying less for their milk than the minimum prices set by the order. They can also expect steady supplies of milk the year-round. Milk handlers thus can focus inwardly to concentrate their efforts on improving plant and marketing efficiencies to compete for larger and more profitable shares of the market. The program also helps assure consumers of an adequate supply of milk throughout the year at reasonable prices to meet their needs.

### **Development of Milk Orders**

The first steps in the development of a Federal milk order are usually taken by cooperative associations representing dairy farmers who are supplying milk for fluid distribution in a particular area. Terms of an order are developed through public participation in hearings held before an order is issued. Producers, handlers, and consumers, or their representatives, may make proposals and take part in these public hearings by providing information on the need for an order and what its provisions should be. The public hearing offers an opportunity for all interested persons to bring their views to the attention of the U.S. Department of Agriculture and to show how they would be affected by any proposed marketing order.

The responsibility of the U.S. Department of Agriculture in developing milk orders is to evaluate the various proposals in the public interest and to resolve any differences. If the Secretary of Agriculture determines that the hearing evidence demonstrates a need for an order, he issues an order under the authority of the Agricultural Marketing Agreement Act of 1937, as

amended, (7 U.S.C. 601-674). USDA's *Rules of Practice and Procedure* (7 CFR Part 900) set forth the procedures for establishing an order.

### **Major Characteristics of Orders**

The Agricultural Marketing Agreement Act specifies the terms a milk order may contain. Each order includes provisions for a classified pricing plan, a system of minimum class prices, and a plan for payment of uniform prices to producers and provisions for administering the order. Although an order considers the particular requirements of an individual market, it is closely coordinated among all markets.

A classified price plan provides different classes and prices for milk in different uses. Milk used in fluid products is placed in Class I, the highest priced class. Milk used in various manufactured products is placed in lower priced classes. In many orders, Class II includes the so-called "soft" products, such as cottage cheese, ice cream and yogurt, while Class III includes "hard" products, such as butter, cheese and nonfat dry milk. A few orders include all manufactured products in a single class.

Each milk order sets forth minimum prices that handlers must pay producers or associations of producers according to the way the milk is used. Such price levels reflect local and general economic conditions affecting the supply and demand for milk. Prices are established for milk of 3.5 percent butterfat content, and adjustments are made for milk that has a butterfat test above or below that amount. Also, many markets get milk from wide areas and prices are adjusted to reflect milk values at different plant locations.

The order provides for the payment each month of a uniform or "blend" price to producers. Most areas use

market-wide pooling—that is, the price to producers is an average of the total class-use value of all milk in the market. All producers in the market are paid the same uniform price per hundredweight (45 kilograms). Several small markets use individual handler pools, where a uniform price is computed for each handler based on his own class-use value of milk. Under handler pooling, all producers selling milk to a particular handler are paid the same uniform price.

Each milk order is administered by a market administrator who is an agent of the Secretary of Agriculture. The market administrator's main duty is to assure that handlers properly account for their milk and pay producers and associations of producers according to provisions of the order. The administration has a staff that makes investigations and audits handler's records to determine that the required payments are made to producers. Handlers are required to make monthly reports to the market administrator.

While Federal milk orders are an important marketing tool, they, by law, serve only a limited function in the marketing of fluid milk. They do not control production, nor restrict the marketing of milk by producers. They do not guarantee farmers a market with any buyer. The orders do not establish sanitary or quality standards. (Sanitary regulations for milk sold in fluid markets are prescribed and administered by local and State health authorities.) The orders do not guarantee a fixed level of price to producers nor do they set a ceiling on producer prices. They do not set wholesale or retail prices.

The Agricultural Marketing Agreement Act of 1937 and its predecessors—the Agricultural Adjustment Acts of 1935 and 1933—insofar as they relate to milk, grew out of the needs of milk producers for help in achieving and maintaining some degree of bargaining power over the prices they received for milk. The characteristics of milk cause an inherent instability in milk marketing and contribute to producers' bargaining difficulties. Milk is bulky and perishable and must be moved promptly to market. Because milk is produced every day of the year, farmers must continue shipping it to market, even when market prices are not satisfactory.

Milk production varies widely with the seasons. Because of the biological process, cows produce more milk in the spring and much less in the fall. Therefore, when there is enough milk in the fall to meet demand, there is too much in the spring.

The demand for fluid milk is relatively stable measured season to season but varies considerably measured day to day. Because of its perishable nature, milk cannot be stored to balance the peaks and troughs of supply. The industry, therefore, must continually produce an oversupply or reserve to make sure there will be enough fluid milk at all times for the day-to-day needs of consumers. Reserve milk that is not needed for fluid use is manufactured into dairy products. But milk utilized in manufactured products returns a lower price to producers than milk used for fluid purposes. Producers, therefore, are interested in getting a maximum proportion of their milk into the higher valued fluid uses, and, in the absence of regulation, often make uneconomic price concessions to achieve that end.

## **Cooperative Efforts**

As early as 1910, producers in some markets had banded together into cooperative associations to gain bargaining power over prices for their milk. Impetus was given to the cooperative movement by the Clayton Act of 1914 and the Capper-Volstead Act of 1922, which established the legal right for producers to market their produce jointly without being held in violation of the antitrust laws.

During the early years, the cooperative associations attempted to bargain with milk handlers for a flat price for all milk, regardless of use. However, the pressure of reserve supplies, normal to the fluid milk industry in the spring, led to a breakdown of the flat price plan. Some handlers refused to take this excess milk from producers at the flat price because it had a lower value when converted to manufacturing uses. Handlers with excess milk tried to dispose of it by increasing consumer sales. Such handlers would offer fluid milk to all or some of their customers at prices lower than those of competitors. Then they would lower the flat price paid to producers. Members of cooperative associations, rather than all producers in the market, often were affected the most by these adverse marketing practices.

The post-World War I era, with the advent of stricter sanitary regulations for milk for fluid use compared to those for manufactured products, accentuated the problems of flat pricing for a perishable product with a pronounced seasonal pattern of production.

In an effort to promote stability in milk markets, cooperatives next developed the "classified price system." This system was in effect in a number of the larger markets in the country by about 1920. Along with

the classified price plans, various pooling arrangements were used.

The cooperative-sponsored price plans were not entirely successful. Success depended upon participation by all groups in the market and there were advantages in remaining outside of the voluntary pricing arrangements. Handlers with a large proportion of fluid milk sales were in a position to offer producers a price above that which cooperatives could pay to their members. These handlers also benefited because their price for milk in fluid uses was less than it would have been under the cooperative's classified price plan. Thus, some producers and handlers did not join in the efforts to operate market-wide programs.

During the 1920's, however, relative prosperity in the cities and increasing sales of milk made it possible to apply these plans with at least partial success. Then, when the economic depression of the early 1930's struck, these voluntary plans broke down under the price competition from noncooperators. The depression did not create the basic problems faced by farmers in marketing their milk. It merely accentuated the problems of existing classified pricing and pooling schemes.

## **Federal Government Intervention**

In the early 1930's, Congress authorized emergency programs for many segments of the economy. Under the Agricultural Adjustment Act of 1933, a program of "licenses" was developed to assist dairy farmers. All milk dealers in a given market were required to pay producers on a classified price basis, and to pool the returns to farmers either on a handler or market-wide

basis. The Act of 1935 set forth more specifically the terms and provisions that could be used under the program and called the instruments "marketing orders" instead of licenses. The Agricultural Marketing Agreement Act of 1937—while largely a restatement of the provisions relating to marketing agreements and orders of the Act of 1935—provided a framework for long-run price and marketing stability. This turned the program to dealing with the problems associated with the inherent instability in milk marketing rather than the severe income problems that arose with the depression. Also, a supply-demand pricing standard was adopted to replace the earlier standard based solely on parity.

### **Changing Conditions Shape the Program**

In the early years of the Federal milk order program, economic conditions for all dairy farmers had been so unsatisfactory that the problem of improving prices for farmers overshadowed all other objectives.

The depression of the 1930's had resulted in reduced consumer purchases and an accompanying surge in milk production. Emergency measures were taken by the Government to raise the prices of both fluid and manufacturing milk. Government officials knew that higher prices might intensify the surplus problem, but emergency conditions outweighed the function of price as a regulator of supply and demand. In 1933, Government purchases of surplus dairy products were begun to support the level of prices paid farmers for milk and butterfat. In 1938, when milk production increased 4 billion pounds over the previous year, Government purchases amounted to 3 billion pounds of whole milk equivalent.

It soon became evident in Federal order markets that a program of increasing milk prices in any market, already oversupplied with milk, could not be continued indefinitely and increased attention was paid to long-run objectives. Attempts were made to establish price levels that would result in a reasonable adjustment of supply and sales in each market. However, the surpluses built up in some markets made it impossible to adjust prices quickly to a level that would bring the supply of milk in line with demand without impacting on the welfare of thousands of dairy farmers.

Formula pricing of Class I (bottling) milk was introduced, and some price changes in line with changed economic conditions were accomplished by these early formulas. The rapidly changing pattern of the early 1940's, with the high level of industrial activity and rising price level, stimulated an interest in the development of a more automatic method of reflecting the supply-demand pricing standard set forth in the Act. Excess supplies disappeared quickly in the face of increasing wartime demands, and the problem soon became one of inducing sufficient production to satisfy market needs for milk.

Then came wartime measures to allocate the Nation's resources. Price ceilings were imposed in 1942, and in 1943 Government incentive payments were made to encourage milk production. Price was again stripped of its supply-demand function in order to prevent runaway inflation. During this period, Federal milk orders continued to function as market-wide pricing systems in a number of markets. The levels of class prices remained relatively constant and changed only as national price objectives were revised. Although price levels played

a lesser role in the program, the classified pricing and other provisions of Federal milk orders continued useful for maintaining an effective system of marketing milk in about 30 markets.

During the past 30 years, there have been a number of dramatic structural and marketing changes in the dairy industry. Economies of scale, new technology and capital investments were among a complex set of forces which resulted in fewer and larger operating units at the farm, processing, and distribution levels. One of the dramatic changes that contributed greatly to this was the increased mobility of milk. Better highways, advances in refrigerated transportation equipment, and the development of improved milk handling methods—including the conversion to bulk tank units and the shift to nonreturnable milk cartons—permitted the movement of bulk and packaged milk over long distances. It is not unusual for bulk milk to be shipped more than 1,500 miles to an area short of milk.

A gradual shift from Grade B to Grade A milk has further expanded the milk supply for the fluid market. Grade A milk as a percentage of total marketings increased from 63 percent in 1955 to 83 percent in 1979. A number of factors encouraged this conversion, including relative prices for Grade A and Grade B milk, bulk tank assembly and standards for manufacturing grade milk that have come much closer to Grade A milk standards. There also has been an erosion of many local health barriers which greatly broadened the supply and distribution areas for milk and dairy products. Plant operators encouraged their producers to convert to Grade A production because plant efficiency is improved by the elimination of the duplicate

receiving systems necessary to segregate Grade A and Grade B milk.

Since the 1950's, dairy farmers recognized the need for centralized management of milk supplies to deal with the pressures of increasingly mobile milk supplies. Although cooperative organizations grew in size and joined together in federated organizations, milk supplies not under their control continued to create disorder and cause a lowering of prices paid to dairy farmers. This pressure was increased during periods of heavy milk production. Dairy farmers, through their cooperatives, continued to seek Federal milk orders as a means of maintaining their prices at reasonable levels.

In 1955, there were 63 Federal milk marketing orders in effect. The number of orders reached a peak of 83 in 1962. Even though new orders were later established, mergers reduced the number to 47 by 1980. During that year, about two-thirds of all the milk marketed in the United States, and about 80 percent of the Grade A milk, were regulated under Federal milk orders.

### **Court Review**

Milk orders issued under the authority of the Agricultural Marketing Agreement Act have often been reviewed by the courts. The constitutional authority for the Act and the validity of the New York and Boston milk orders issued under its authority were upheld by the Supreme Court in *United States vs. Rock Royal Cooperative, Inc.*, 307 U.S. 533, and *H. P. Hood and Sons vs. United States*, 307 U.S. 588. The power of Congress to regulate the intrastate transactions that directly affect interstate commerce was confirmed by the Supreme Court in *United States vs. Wrightwood Dairy*

## Procedures for Developing and Issuing Federal Milk Orders

Co., 315 U.S. 110. Various aspects of individual milk orders have been subjected to review by the courts.<sup>1</sup>

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<sup>1</sup>Queensboro Farm Products v. Wickard 137 F. 2n 969 (1943), Stark v. Wickard 321 U.S. 288 (1944), Stark v. Brannan 342 U.S. 451 (1952), Lewes Dairy, Inc., v. Hardin 401 F. 2d 308, Certiorari Denied, 394 U.S. 929 (1969), Dairymen's League Cooperative Association v. Brannan 173 F. 2d 57, Certiorari Denied, 338 U.S. 825 (1949), Lehigh Valley Coop. Farmers v. Benson 370 U.S. 76 (1962), Allen, Russell, et al. v. Freeman 396 U.S. 168 (1969), Dairylea Cooperative, Inc. v. Butz 504 F. 2d 80 (1974), Lamers Dairy v. U.S. 500F. 2d 34 (1974), Benz v. Hardin 32 AD 824 (1973), Carnation v. Butz 372 F. Supp 883 (1974). Also, see December 1977 Agriculture Decisions, Cumulative List of Court Decisions, 36 AD 2139 through 2166.

### Government and Industry Roles

The Agricultural Marketing Agreement Act of 1937, as amended, authorizes Federal milk orders and defines the role of Government in carrying out procedures for their development and issuance. USDA is responsible for judging the merits of proposals made at public hearings. Following standards prescribed in the Act, it must resolve the problems presented and administer the orders after they are issued. The U.S. District Courts have authority to enforce the orders.

Since the purpose of a milk order is to provide dairy farmers with a marketing plan under Government supervision and the issuance of an order requires approval by the farmers affected, farmers usually take the first steps in proposing an order. The Act does not suggest that milk orders be made available only to markets in which producers are organized. However, objectives and machinery of the program are such that the orderly and systematic representation of producers in a marketing cooperative is almost essential for the establishment and operation of a marketing order.

Handlers are encouraged to take an active part in promulgation and amendment proceedings. They have direct knowledge of many competitive conditions in the market that individual producers or cooperative associations are not in a position to know. Active participation by handlers enables USDA to develop an order better suited to the existing marketing conditions.

Public participation is also encouraged. USDA makes a special effort to keep consumers informed about public hearing dates and program proposals of orders which may have a significant impact on them.

Although much of the language of Federal orders is technical by nature, USDA aids consumers by preparing explanations of proposals in easy-to-understand language to accompany the proposals.

### **Conditions Indicating Need for an Order**

In an unregulated market, problems may exist which can be alleviated by a milk marketing order.

A cooperative association may negotiate a system of classified pricing with some of the handlers in an unregulated market. However, other handlers may undermine the cooperative's bargaining position by temporarily offering unorganized producers a flat price above the blend or average price paid cooperative members under the negotiated classified pricing plan. This encourages members to leave the cooperative and discourages non-members from joining. Organized producers lose bargaining strength, and eventually the position of all producers in the market is weakened.

A general weakness of producers' bargaining position often results in prices generally lower than those paid in surrounding markets. In time, such depressed prices may drive enough producers from the market to threaten a shortage of fluid milk.

Unequal bargaining strength or lack of coordination between producer groups may indicate general weakness in the bargaining position of all producers in the market. Often price concessions won by handlers in bargaining with one producer group are used as a lever to lower the prices paid another group. Also, some handlers may refuse to accept all or part of the milk offered by producers who have been their normal suppliers even though

substitute supply sources, under equal bargaining conditions, would be no more economical.

Handlers may sometimes use special premiums or deductions to discriminate between producers. Considerable unrest can develop when different producers get different prices for the same grade of milk.

In the marketing system for fluid milk, payments are normally prearranged, but are not made until several weeks after producers have made deliveries. Thus, confidence of buyers and sellers is essential to the smooth functioning of such a system. Lack of information about the market and absence of an impartial agency to appraise buying practices used may leave a void in which mistrust in the marketing system leads to practices that disrupt orderly marketing.

None of the conditions cited should be regarded as a "prima facie" indication of the need for an order. The extent to which the different conditions disrupt the orderly marketing of milk varies, and the conditions themselves vary in degree.

### **Findings Relative to Interstate Commerce in Milk**

The Agricultural Marketing Agreement Act specifies that orders "shall regulate, in the manner . . . provided, only such handling of . . . (milk) . . . or product thereof, as is in the current of interstate or foreign commerce, or which directly burdens, obstructs, or affects, interstate or foreign commerce in such commodity or product thereof." In some areas, milk associated with a particular market may not be moving across state lines. Nevertheless, the price competition that still exists between such milk and milk supplies

in other states has been considered as affecting interstate commerce.

The extent to which milk handling must affect interstate commerce to support an order is not, according to the Supreme Court of the United States, "a technical legal conception but a practical one, drawn from the course of business." Interstate commerce in milk has expanded considerably in the past 30 years or so. Technological developments affecting the milk industry of the nation have broadened marketing areas for milk, and the products of milk are generally distributed in a nationwide market.

## **Pre-hearing Procedures**

USDA's *Rules of Practice and Procedure* prescribe pre-hearing procedures. A new marketing order is normally proposed by dairy farmers, but it may be proposed by any person, including the Secretary of Agriculture. The proposal and written request for a public hearing on the proposal are submitted to USDA. Upon receiving the proposal, USDA makes an investigation. If it shows that the proposed marketing order will not carry out the policy of the Act or, for other proper reasons, shows that a hearing should not be held on the proposal, the request is denied. The petitioner is notified and provided a statement of the grounds for the denial. If USDA concludes that the proposed marketing order will carry out the policy of the Act, a notice of hearing is issued after providing the industry and public an opportunity to submit additional proposals.

Usually, a proposal for a hearing on a new order is made by a cooperative association representing producers who supply milk to the marketing area for which the regulation is sought. The producer group

usually leads in arranging meetings before a proposed order is drafted to acquaint others in the area with the program. County agricultural agents often assist the producer association by explaining the general purposes of the Federal milk order program and how it operates. For larger meetings, a specialist in dairy marketing is sometimes called from the Cooperative Extension Service to assist in this educational phase of the program development. Also, USDA specialists associated with the program help prepare material about milk orders and, in some cases, attend meetings to explain the purposes and operations of the orders.

When USDA receives a proposal for a new order, it is handled by the dairy division of the Agricultural Marketing Service. This division is responsible for investigating each hearing proposal and recommending that a hearing on the proposal be called or denied. One or more marketing specialists are assigned to study the proposal and the marketing conditions in the proposed area.

Practical and economical administration of the program requires that expenditure of time and money by Government and industry in public hearings be preceded by sufficient preliminary studies in the interest of economy. The exact nature and extent of the pre-hearing study varies with individual circumstances. Sometimes the need for a hearing may be obvious, but in other cases the market disturbance may be less evident on the surface. If it is obvious from the investigation that the proposed order would not carry out the policy of the Act, no hearing is held.

During the course of most pre-hearing investigations, the marketing specialist consults with handlers and producers and is available for

consultation upon request of any interested persons. Such conferences often include representatives from several markets when mutual marketing problems arise. Whether in connection with a proposal for a new order or an amendment to an existing order, it is helpful to have discussions between industry members and USDA representatives about the marketing problems. All such conferences, however, must be concluded before a hearing notice is issued. After that, and until USDA reaches a final decision on the proposal, discussions on the merits of the proposals are prohibited by law between industry members and those in USDA who help decide whether the proposals should be adopted. Procedural matters may be discussed at any time.

Before recommending a hearing on a proposed new order, USDA must be satisfied that:

1. Marketing conditions in the area could be improved by a milk order.
2. Evidence pertinent to the consideration of a milk order will be forthcoming at the hearing.
3. The proponents of the order appear to have the support of a substantial number of producers in the market.

Information gathered by USDA during the pre-hearing study may not be used after a hearing in deciding how to resolve any of the marketing issues. An order and its provisions must be based solely on the evidence introduced at a hearing.

If it appears from the inquiry that a proposed order is feasible and that proponents are prepared to present evidence on the need for an order, the director of the AMS dairy division in USDA recommends that a hearing notice be issued. The formal notice of hearing must be published in the Federal Register at least 15 days

before a hearing, but a longer period is usually provided. The official notice gives the time and place at which the hearing will be held and contains the proposals to be considered.

These pre-hearing activities relate to the procedure followed before a hearing on a proposed order for a new area. The procedures are similar, in most respects, for hearings on proposed amendments to an established order, but there are a few differences. Three days' notice of the hearing is required on certain types of proposed amendments, although more time is normally provided. A proposed order for a new area is normally sponsored by a producer group, but proposed amendments are often sponsored by handlers as well. If the proposed amendments relate only to a few issues, the pre-hearing procedures may be relatively simple.

## **The Public Hearing**

A public hearing is held to receive evidence about economic and marketing conditions that relate to the handling of milk in the marketing area for which a Federal milk order is proposed. Evidence may be presented by any person on any of the proposals contained in the hearing notice. Except for appropriate modifications, only the proposals in the notice may be considered at the hearing.

The hearing is held in the market for which the order is proposed. This helps those persons who would be affected by the order to participate in the hearing process.

The hearing is conducted by an administrative law judge. Currently, there are five administrative law judges in USDA. These judges can be removed only for cause, and their

office operates as a separate unit within USDA. Although they preside over Federal order hearings, they do not issue the decisions in these rulemaking proceedings.

At the hearing, the administrative law judge determines the order in which witnesses are to appear and rules on procedural questions that may arise. If an objection to the judge's ruling is made, the Secretary may later reverse the ruling after reviewing the hearing record.

Interested persons who desire to testify are given an opportunity to be heard on matters relevant to the issues under consideration. Questioning of witnesses is permitted to clarify facts in their testimony. In most instances interested persons can develop their own case better by presenting a direct statement rather than by cross-examination of another witness. Witnesses also may refuse to answer questions. While testimony is strictly voluntary, refusal to answer questions may affect the weight to be given statements. All the testimony at the public hearings is taken under oath or by affirmation and is reported verbatim.

A marketing specialist familiar with the marketing conditions in the particular area and the operation of milk orders is assigned by the dairy division to each public hearing. The specialist is responsible for getting in the record as much relevant information as possible. The specialist follows the testimony of the witness carefully to note any omission of information pertinent to the consideration of the issue, and an attempt is made through cross-examination to elicit such information or to clarify the testimony when it is apt to be confusing upon review at a later date. The specialist directs the preparation of statistical

exhibits and other pertinent data that are readily available to USDA and introduces this material in the record. It is the responsibility of the specialist to be sure the record reflects adequate data upon which a decision at USDA can be based.

Where expert testimony of a special type may be needed, a marketing specialist is sometimes assigned to testify about order provisions. Such assignments are usually limited to factual testimony concerning a provision, and the specialist does not appear as an advocate or opponent.

An attorney from USDA's Office of the General Counsel is usually assigned to each hearing and shares with the marketing specialist the responsibility for eliciting information for the record. The attorney also represents USDA on questions of a legal nature that may arise.

The principal participants at the hearings are representatives of producers, handlers, and consumers who appear as witnesses. Based on their technical knowledge of the market, handlers and producers present evidence of marketing conditions in the area. Consumers, who may appear as individuals or as representatives of consumer groups, present their viewpoint.

Because the hearing record is the source of information upon which the dairy division must make a recommendation, it is imperative that each record presents the facts completely and clearly. Except for official documents, the public hearing record is the sole source of information for appraising the issues. But official notice is limited. For example, notice may be taken of the provisions in another Federal milk order, but not of the marketing conditions in the other area that called for such provisions.

Data necessary to evaluate the terms of a proposed milk order include a broad field of information. Evidence considered pertinent to the consideration of a milk order relates to marketing, price and bargaining problems, interstate commerce, marketing institutions, the characteristics of the marketing area, classified pricing systems in effect in the marketing area, health requirements applicable to milk and its products, transportation systems, pooling and all other factors affecting supply and demand conditions.

At the close of the hearing, the administrative law judge sets a time period within which written briefs may be filed by interested persons. Such persons may suggest to USDA the conclusions the Secretary should reach on the basis of all the hearing evidence. The briefs must refer only to evidence presented at the public hearings and may not offer new facts for consideration.

After the hearing, the administrative law judge scrutinizes the verbatim record and certifies it as a true and correct record. The record is then turned over to the dairy division for study and preparation of a recommendation on the issues.

### **The Recommended Decision**

Because the marketing of milk is complex, regulations must be drafted to accomplish the purposes of Federal milk orders under many diverse situations. To afford dairy farmers, milk handlers, and the general public an opportunity to appraise the potential effect of a proposed milk order before it is drafted in final form, a recommended decision and tentative order are issued by the Administrator of the Agricultural Marketing Service after an analysis of the evidence introduced at the public hearing. The

time between the close of the hearing and the issuance of the recommended decision varies considerably, depending on the complexity of the issues involved. Interested persons are given an opportunity to consider the proposed order and file written exceptions to the findings and conclusions of the decision and the provisions of the recommended order.

USDA's *Rules of Practice and Procedure* requires issuance of a recommended decision and says it should contain:

(1) A preliminary statement containing a description of the history of the proceedings, a brief explanation of the material issues of fact, law, or discretion presented on the record, and proposed findings and conclusions with respect to such issues as well as the reasons or basis for them;

(2) A ruling upon each proposed finding or conclusion submitted by interested persons; and

(3) an appropriate proposed marketing agreement or marketing order effectuating the recommendations.

The recommended decision is prepared by marketing specialists in the dairy division after careful study of the record and appraisal of the issues. After the decision has been reviewed and approved within the dairy division, and for legal sufficiency by the Office of the General Counsel, it is transmitted to the Administrator of the Agricultural Marketing Service for review, approval and issuance.

The recommended decision is published in the Federal Register and also mailed to everyone known to be interested in the proceeding. The decision specifies the period of time within which written exceptions may be filed by interested persons.

Exceptions must be based on the facts contained in the hearing record. Exceptions provide the opportunity for a review of USDA's tentative conclusions by interested persons.

In emergency situations, where time does not permit the issuance of a recommended decision, the regulations provide that this step in the procedure may be omitted. The emergency omission of a recommended decision applies in practice only to amendments, not to new orders.

### **The Final Decision**

After exceptions to the recommended decision have been received, the dairy division re-examines the findings and conclusions contained in the recommended decision in light of the exceptions and the hearing record. A final decision is then drafted and transmitted to the Secretary for his review, approval and issuance.

The final decision, as in the case of the recommended decision, must be based on the statutory standards for milk orders. The decision includes a statement of USDA's findings and conclusions and the complete text of the proposed order. It sets forth the reasons for accepting or denying proposals advanced at the hearing and includes rulings on exceptions to the recommended decision. The provisions of the order contained in the decision represent USDA's final proposed regulations and are the provisions presented to producers for their approval.

The Agricultural Marketing Agreement Act requires that handlers be given an opportunity to enter into a voluntary marketing agreement containing the same terms and provisions set forth in USDA's

proposed order. This agreement is also contained in the final decision. In the past, handlers have usually failed to sign these marketing agreements. However, the order may be made effective without the agreement if the Secretary determines that the failure of handlers to sign the agreement obstructs the purposes of the Act, and that issuance of the order is the only means of advancing the interest of producers.

### **Producer Approval**

Producers must approve a new order or an amended order before it may be issued. Producer approval of a new order must be determined by referendum. To be approved, a new order must be favored by at least the required percentage (defined below) of the eligible producers voting in the referendum. Producer approval of an amended order may be determined by referendum or by the polling of cooperatives that may vote for their entire memberships. The referendum or cooperative polling are conducted by an agent of the Secretary of Agriculture.

A producer's eligibility to vote is determined by his affiliation with the market during a representative period. This is usually the latest delivery period for which the necessary records of producer deliveries are available.

Orders that provide for market-wide pools must be approved by referendum by two-thirds of the eligible voting producers, or by producers who supplied two-thirds of the milk sold in the defined marketing area during a designated representative period. If the order establishes an individual handler pool, the order must be approved by referendum by three-fourths of the eligible voting producers or by producers who supplied three-fourths of the milk. If

approval is determined by polling of cooperatives, two-thirds of all eligible producers on a market with a market-wide pool or three-fourths of all eligible producers on a market with individual handler pooling must favor an amended order before it may be made effective.

The Agricultural Marketing Agreement Act provides, if the association so requests, the vote of an approved, bona fide cooperative association must be accepted by the Secretary as the vote of all members of the association who are eligible to vote on a prospective order. This is commonly referred to as "bloc voting." A cooperative may bloc vote its membership on all questions involving new and amendatory orders except when voting on Class I base plan provisions. Producers must vote individually on Class I base plan provisions.

The determination of the cooperative's eligibility to bloc vote its membership is made by the director of the dairy division. This determination is based upon information contained in an application filed by the cooperative, including evidence that the cooperative is controlled by its members and is engaged in marketing members' milk.

Bloc voting—claimed by some people as giving cooperatives too much market power—has been justified on several conditions. At the outset of the program, it was felt that bloc voting would prevent proprietary handlers from attempting to coerce individual producers into voting against a milk order. Bloc voting enables the members of a cooperative to take unified action on matters of vital importance to them, and thus gives a degree of strength to cooperatives that they would not otherwise have.

The relationship between farmers and their cooperative is another consideration as far as bloc voting is concerned. A farmer who joins a cooperative association, transfers to the cooperative responsibility for marketing his milk. Farmers commit all their production to the cooperative and the cooperative is committed to finding the best available market for all the milk its members produce. Since Federal orders are an important tool which cooperatives use in marketing members' milk, it is reasonable that the cooperative be able to vote on behalf of its entire membership on proposed orders or amended orders.

Except when voting on a Class I base plan or an advertising and promotion program, producers must accept or reject the entire order, whether new or amended, that was adopted. In developing a new order or amending an order, the Secretary is required by law to adopt only those provisions that are based on the public hearing and that are in the public interest. There would be no assurance that the Secretary could carry out his responsibilities if producers were allowed to select only the provisions or amendments they desire.

The law requires that Class I base plans and advertising and promotion programs be voted on separately from the rest of the order. Disapproval of these provisions by producers does not affect the remaining order provisions.

### **The Order or Amended Order**

The Secretary issues the order if the proposed order or amended order is approved by the required number of producers. Handlers are then required to operate in compliance with the terms and provisions of the order.

In new orders, the pricing provisions are usually made effective after the handlers have been given time, usually one month, to observe the recordkeeping provisions of the order in action.

The order thus promulgated remains in effect until an amended order has been developed through the same procedures. However, in emergency situations, the order, or certain terms and provisions it contains, may be suspended or terminated.

### **Suspension or Termination**

Actions suspending particular provisions may be taken without following the usual procedures involved in amendatory actions. Provisions are suspended only when there is an imperative and clear need for emergency action and time will not permit the more lengthy requirements of an amendatory proceeding. Customarily, USDA seeks the views of interested persons before deciding whether the order provisions in question should be suspended. Provisions are normally suspended for no more than several months.

The Secretary may terminate an order or provisions of an order if he finds they no longer accomplish the purposes of the Act. An order must be terminated at the request of a majority of producers supplying the market, if such majority produces more than half of the market's milk supply.

### **Administrative and Legal Recourse**

The Agricultural Marketing Agreement Act authorizes a handler to challenge an order, any of its provisions, or any obligation the order imposes; and to ask to have it modified or to be exempted from it.

Such a challenge is made before a USDA administrative law judge who in these cases represents the Secretary of Agriculture. The judge holds a hearing and makes a determination whether the order provisions or their application are in accordance with the law. The decision of the judge may be reviewed by the USDA's judicial officer.

A handler not satisfied with the results of this administrative remedy may challenge USDA's decision in court. The first court review is made in the appropriate Federal District Court, but the matter ultimately may be reviewed by the Supreme Court. If USDA has determined that an order provision is legal and being correctly applied, the handler remains subject to that provision while USDA's decision is pending review by the courts, unless interim relief is granted by the judicial officer of USDA.

The Supreme Court of the United States held in *United States vs. Ruzicka*, 329 U.S. 287, that these procedures are the exclusive means whereby an order provision or obligation under it can be tested by a handler. In other words, a handler must pursue the administrative remedy according to the procedures established in the Act, which provide for a hearing and decision by the Secretary of Agriculture prior to review of the issue in the District Court. Following this principle the courts have, in all but a few instances, refused to listen to a handler's challenge of the legality of an order provision or an obligation imposed upon him in any enforcement action initiated by USDA.

In the first decade of Federal milk order regulations, producers were given standing in court only in a very limited situation. The Supreme Court

## **Principal Provisions of a Federal Milk Order**

ruled in the late 1940's that producers could bring an action against the Secretary only in the circumstances where they were contesting the distribution of the total pool value among producers. This limitation on producers challenging order provisions prevailed until the late 1960's. At that time, the liberalization of standing in other areas extended into Federal milk order litigation. Since then, producers have been awarded standing in any area where they could demonstrate that the issue raised is within the "zone of interest" to be protected. Now, producers need only show that they have been adversely affected by a regulation to get official recognition before a court.

Because milk orders are legal instruments that obligate handlers to pay minimum class prices for milk purchased from farmers, they must be detailed and explicit. The thrust of the many provisions in a milk order is to define those who are obligated under the order and the exact terms of the obligation.

### **Marketing Area**

The definition of the marketing area is the first important term of an order. Order regulations apply to the purchase of milk by handlers when they sell milk in a designated marketing area. Under the present orders, marketing areas differ considerably in size. Some may consist of only a few counties, while other marketing areas may include a major part of some of the larger states, or parts of several states.

The marketing area is designed to include all of an area where the same milk distributors compete with each other for sales of milk. Because only handlers doing business within the defined area must pay the minimum prices set by the order, it is important to draw the boundary line at points where there are relatively few route sales moving across the boundary. This objective has become increasingly difficult to attain in recent years. Fluid milk distribution business has expanded over much wider areas, with considerable overlapping of delivery routes. Improved refrigeration and transportation, the use of single-service paper and plastic containers, and the heavy reliance on supermarkets have encouraged this expansion of sales areas.

Many areas that were once generally distinguishable as separate markets now overlap in terms of distribution routes and procurement of supplies. Large-scale distribution over

wide areas has introduced new dimensions to the problem of assembling milk supplies. As a market reaches out greater distances for its milk supplies, neighboring farmers often find themselves receiving substantially different blend prices because they are delivering to different order markets. Such situations have led producers to ask that separately regulated areas be placed under one order. The area of milk procurement has become increasingly important in determining marketing area definitions.

### **Handler**

Milk "handlers" are the only persons regulated under a Federal milk order. Under most orders, a handler is any milk dealer whose plant is approved by a duly constituted health authority and who disposes of Grade A fluid milk products in the defined marketing area. Handlers include fluid milk processors who distribute milk to consumers and retailers, and also persons who sell milk to other milk dealers for fluid distribution. The term "handler" applies to proprietary operations (individuals, partnerships, or corporations) and also to cooperative associations that handle the milk of their members.

The definition of a handler and the application of order regulation would be relatively simple if all handlers did business in the same way and if the marketing area boundary could be drawn at the exact point where sales routes end. All handlers in this situation would be completely regulated and pay the minimum established prices for milk bought from farmers.

The handling of milk for fluid markets does not fit one mold, and the regulation, if it is not to stifle normal economic development, must recognize the characteristics of the

industry. Production and distribution efficiencies have created many cases where handlers are distributing milk in more than one Federal order marketing area from the same plant, so a decision must be reached as to which order shall apply. Most orders provide that handlers shall be regulated by the order for the marketing area where they have the greatest Class I sales. Such handlers are defined as fully-regulated handlers under that order.

Handlers who are not fully-regulated are defined as either partially regulated or exempt handlers. Partially-regulated handlers are those with only small fluid disposition in the regulated sales area. Usually, their principal business is the production and sale of manufactured products, or fluid sales in unregulated areas. Exempt handlers may be small operators, such as producer-handlers who process only the milk from their own dairy herds or state governments that operate milk plants.

### **Producer**

A producer, as defined in most orders, is a dairy farmer who delivers to a fully-regulated handler milk that is approved for distribution in the regulated market in the form of fluid milk products.

### **Classified Pricing**

An order establishes prices by classes according to the use of milk. Milk used for fluid consumption is priced separately at one level, while the remainder is priced at a lower level or levels in line with the value of the manufactured dairy products made from such milk.

Because milk is perishable and is subject to contamination, costly sanitary measures must be taken by

dairy farmers to assure that the milk going into fluid uses is of high quality when it leaves the farm. Also, because it is bulky, there is a high cost involved in hauling raw milk long distances to city processing plants. These conditions make milk approved for fluid consumption cost more than milk that can be used only for manufacturing purposes. A higher price must be paid to encourage its production and delivery to fluid milk outlets.

Also, sales of fluid milk are generally even the year-round, while production is seasonally higher in the spring than in the fall. When producers deliver enough milk in the fall to meet fluid consumption, they usually deliver more than is needed for fluid use in the spring months. Classified pricing accommodates the need to price these reserve milk supplies for the fluid market at the lower manufacturing value to assure their orderly disposal.

Most of the milk orders establish three use classifications—Class I for fluid uses, and Class II and Class III for manufacturing uses. Several orders include the manufacturing uses in a single class.

Class I uses generally include products packaged for fluid consumption such as whole milk, skim milk, lowfat milk, buttermilk, and flavored milk drinks. In the three-class orders, Class II usually includes cream, yogurt, cottage cheese, and ice cream, while Class III includes butter, cheese, and non-fat dry milk.

### **Allocation of Milk to Classes**

The class prices established by an order apply to “producer milk” delivered to regulated handlers by producers. The amount of such milk used in each class is easily

determined if a handler receives only producer milk. However, in addition to his receipts of producer milk, a handler also may receive milk from other sources, such as from an unregulated plant. It is impossible to determine which milk was actually used in a particular product when producer milk is intermingled in a plant with “other source” milk. This necessitates having certain accounting rules for determining the amount of producer milk that will be priced in each class. A specific allocation procedure, which is generally the same for all orders, is set forth in each order for this purpose.

In general, the allocation procedure assigns unpriced, other source milk to the lowest class. Under limited conditions, milk received by a handler from unregulated supply plants is assigned to the handler’s utilization pro rata with receipts of regulated milk.

Receipts of milk from plants regulated under other Federal orders are allocated differently. Packaged milk is assigned to Class I milk at the receiving plant. Bulk milk received for manufacturing is assigned to the lowest class. Other receipts of bulk milk are allocated to the receiving handler’s utilization in each class.

### **Class Prices**

The policy to be followed in pricing milk under Federal milk orders was established by the Congress and is stated in the Agricultural Marketing Agreement Act. The Act directs the Secretary of Agriculture to establish milk prices that reflect certain economic factors, assure a sufficient quantity of pure and wholesome milk and are in the public interest. A public hearing is held to gather evidence on the supply-demand conditions in an area and on other relevant

economic conditions. The considerations involved in establishing class prices, and the resulting effect upon uniform prices paid to producers, must be appraised in the light of the declared policy of the Act.

The primary standard for establishing Class I prices under the Act is supply and demand conditions affecting the marketing area. The "price of feeds, the available supplies of feeds, and other economic conditions" referred to in the Act are taken into account as they affect prospective market supply and demand conditions. The "public interest" is served by an adequate supply of milk at a reasonable price.

In all Federal order markets, the price for Class I milk is presently based on the value of milk for manufacturing uses plus a specified Class I differential. The values for manufacturing milk depend upon the average price paid for manufacturing grade milk by plants in Minnesota and Wisconsin. Class I differentials were established at levels which, in conjunction with the dairy price support program, will insure present and future supplies of high-quality milk throughout the Federal order system.

The Minnesota-Wisconsin price series is used as the basic mover of Class I prices for several reasons. The M-W price is representative of the price paid for more than half the manufacturing grade milk in the country. Numerous plants in the two states compete for milk supplies. Whenever milk supplies (including Grade A supplies) tighten in distant markets, cooperatives and milk handlers import milk from these two states, thus reducing the milk available for processing and reducing production of products such as butter and cheese. When

milk supplies are plentiful, this shows up in increased dairy product production, lower product prices and lower prices for manufacturing grade milk.

The M-W price is a measure of changes in supply-demand conditions throughout the country. It is arrived at in the marketplace rather than by the Government, although it is influenced by the price support level at times when prices are at or near the price support level.

As long as large quantities of manufacturing grade milk exist in the upper Midwest, it is necessary to coordinate Class I and blend prices in this area with manufacturing grade milk prices. Without coordination, serious marketing problems and inequities between Grade A and Grade B producers develop. Alignment of Class I prices elsewhere with those in the upper Midwest is facilitated by using the M-W price as a mover for Class I prices in all Federal order markets.

Another function is served by the use of the M-W price in establishing or adjusting class prices. It provides coordination between the milk order and price support programs. Both programs are the responsibility of the Secretary of Agriculture and have similar legislative pricing standards. An increase or decrease in the price support level is reflected in the prices paid for manufacturing grade milk, if markets are at or near support levels and, in turn, are reflected in the M-W price, and thus in Federal order prices. Because of this tie-in between the two programs, changes in the price support level can be used to adjust milk prices throughout the dairy economy, including prices established under milk orders.

Factors considered in establishing

Class I differentials include: (1) Additional costs of meeting Grade A sanitary regulations; (2) Costs of transporting milk from areas of production to areas of consumption; (3) The cost of producing milk in the supply area; and (4) Supply and demand conditions for milk, including the cost of alternative supplies.

For any length of time, the level of Class I price in any market generally cannot exceed the cost of buying the milk in another supply area and transporting it to the consuming market. If a price advantage exists long enough for handlers to recognize the advantages of another supply, they will change their buying arrangements. An important guide to the proper level of Class I prices in a given market is the cost of alternative supplies.

Prices for milk used in classes other than Class I must be established at levels that assure the orderly disposal of the milk supplies that are in excess of the fluid milk needs of the market. In determining the level of reserve milk prices, it is important that handlers in fluid milk markets not be unduly encouraged to engage in manufacturing operations by establishing prices for reserve milk supplies lower than the competitive price for manufacturing grade milk. On the other hand, prices cannot be set so high that handlers are unwilling to accept the excess or reserve milk supplies from producers and process it into manufactured products.

Reserve milk prices under the orders are presently based on the general value of manufacturing grade milk. The average price received for such milk by farmers in Minnesota and Wisconsin, in addition to being the basis for all Class I prices, is also the basis for pricing Class II and Class III milk.

## Pooling Returns to Producers

Because different prices apply to milk disposed of in the several classes, a method of pooling, or distributing the total returns from sales of milk among producers at a uniform price, is used in conjunction with classified pricing. The Act provides for a choice of two methods of pooling returns to producers. One is the market-wide pool; the other is the individual handler pool.

Under a "market-wide" pool, the total money value of all milk delivered by all producers to all handlers (pounds of milk in each class multiplied by the minimum class prices) is combined in one pool, and the pool is divided by the total amount of producer milk that is priced under the order. Then, all producers are paid the same "uniform" or blend price per hundredweight (45 kg.) for their milk shipments, except for adjustments to reflect variations in the butterfat content of the individual producer's milk and the location at which the milk was received by the handler.

In an "individual handler" pool, the same computations are made in arriving at each handler's value of milk, and all producers supplying a particular handler are paid the same "uniform" or blend price per hundredweight (45 kg.) (which also is adjusted for butterfat content and location of receipt). Under this method of pooling, producers supplying one handler will receive a uniform price that differs from that paid producers supplying other handlers in the market since the proportion of milk used in the different classes varies among handlers.

Although once used more widely, individual handler pools were applicable only in three Federal order markets in 1979. Major

changes in the marketing of milk have led to their limited use. Individual handler pools usually were in markets that were relatively short of milk, or where the reserve supplies were distributed evenly among handlers. Where supplies were short, this type of pooling served as a means of allocating the available supply among handlers in relation to their fluid sales. The handler with a higher proportion of Class I sales would pay a higher uniform or blend price. That would tend to move producers away from the handler who had a higher proportion of sales in the manufacturing value uses.

Market-wide pools, on the other hand, are best adapted to markets where reserve supplies are unevenly distributed among handlers. In many markets, particularly the larger ones, the reserve supply of milk can be more efficiently handled by consolidating the reserve supply in plants most distant from the market. Often, one reserve plant where milk products are manufactured much of the year will provide the necessary fluid milk for several handlers in the short-production months. This specialization of function would result in lower prices at such a plant under an individual handler pool than those paid by handlers who specialize in fluid sales. In a market-wide pool, all producers who are supplying milk for the market, even if it is needed for fluid use only in the short-supply period, are paid uniformly according to the total market utilization.

The returns to producers who are members of a cooperative association may be distributed among the membership according to the contract between the association and its members. This arrangement, which is commonly referred to as rebrending, is specifically authorized by the Act.

## Price Adjustments

The class prices handlers pay and the prices producers receive are adjusted by butterfat differentials and by location differentials. Butterfat differentials reflect the variations in the market value of milk containing different quantities of butterfat. Location differentials reflect the cost of transporting milk from the production area to the consuming area.

Prices under the various Federal orders are presently determined and announced for milk containing 3.5 percent butterfat. The butterfat differentials are quoted in terms of cents per 100 pounds of milk (45 kg.), and apply to each "point" (one-tenth of one percentage point) of variation from the basic test at which prices are announced.

In some of the larger milk markets, the milk supply is assembled in a system of so-called country plants located in the area of production at varying distances from the city distributing plants. Milk collected at these country plants is then transported in tank trucks to the city plants. Some processing plants, usually those with manufacturing facilities, are also located in the production area at considerable distance from the principal center of consumption.

The minimum prices established by Federal milk orders are normally applicable at the plant at which milk is first received. The pricing plans provide for zone differentials by which the central market price is adjusted to determine a zone price for each plant. Generally, the price declines in succeeding zones as the distance from the center of the market increases. The charge for hauling milk from the farm to the first plant at which it is received is

negotiated between the dairyman and the hauler.

In contrast to the other orders, the New York-New Jersey order establishes prices for most milk at the farm rather than at plants. For accounting and pooling purposes, farm bulk tank milk sold by producers is identified as milk coming from "units" or groups of farms, rather than as milk received at a plant. The farm is considered to be the point of receipt by the handler rather than the plant to which the milk is moved. The class prices charged to handlers for bulk tank milk are announced on an f.o.b. farm basis, with farms zoned by townships and prices adjusted by the same location differentials that otherwise would apply to milk received at pool plants in the same zone.

### **Producer-Settlement Fund**

Some handlers have mostly Class I milk. Other handlers may use a larger proportion of their receipts for manufacturing purposes. This results in wide variations among handlers in the average utilization value of their milk. Under a market-wide pool, handlers are required to pay at least the minimum blend price to all producers from whom they purchase milk. The difference between what the handler pays producers and the utilization value of the milk is paid to or received from a "Producer-Settlement Fund." Handlers with higher than average Class I utilization pay the difference into this fund. This money is then paid out to handlers with lower than average Class I utilization. This results in a uniform minimum price to all producers.

### **Integration of Unpriced Milk into the Classified Pricing System**

In the early years, the orders provided for full regulation of all

plants that distributed any milk in the marketing area. Full regulation permitted a plant and its producers to share in the proceeds of a fluid market, regardless of whether they had a close and regular association with the market. By selling a token amount of milk in the marketing area, a plant could become a pool plant and share in the proceeds of the market even though it took no responsibility in providing milk to the market when needed.

Unlimited participation in a market-wide pool permitted surplus milk from other markets to be shifted to the regulated market. This wide-spread distribution of pool funds to dairy farmers not regularly associated with the market kept the proceeds from the market's fluid milk sales from serving their purpose of encouraging the production of a dependable supply of high-quality milk by producers regularly supplying the fluid market. Thus, the effectiveness of a market-wide pool in providing orderly marketing and adequate milk supplies was being undermined.

It became obvious that it would be necessary to establish performance requirements as a basis for sharing in the proceeds of a fluid market. Such pool plant requirements also could be used as a means of exempting from full regulation handlers having only limited distribution in the marketing area.

Concurrent with setting performance requirements to permit some unpriced milk to enter a marketing area was the need to devise a way to prevent it from entering the market at less than order prices. Obviously, it would be unrealistic to protect the Class I utilization of a market from demoralization from its own excess or reserve milk through a classified pricing system and, at the same time,

allow excess milk from another market to be sold without regulation. If milk from unregulated sources is available to some distributors at less than order Class I prices, distributors who pay order Class I prices would be at a competitive disadvantage. The purpose of the classified pricing plan would be thwarted. Such a situation would create the very disorder the milk order program was designed to eliminate.

All orders contain provisions for the orderly movement of unpriced milk into regulated markets. The current provisions, which are essentially uniform among the orders, were developed after a 1962 decision of the Supreme Court (*Lehigh vs. United States*) nullified certain provisions in the New York-New Jersey order relating to unpriced milk. Those dealing with the treatment of regulated milk moving between Federal order markets also were revised because of the Court's decision and were somewhat uniformly changed.

For milk distributed in a Federal order market from unregulated plants, three options are given to plant operators: (1) Pay the dairy farmers delivering the milk at the same rate they would be required to pay if they were fully regulated handlers. (2) Offset in-area sales by Class I purchases from handlers regulated under any Federal order. (3) Pay to the producer-settlement fund the difference between the Class I and blend prices of the order on their in-area sales. These options are designed to place plant operators, who are defined as partially regulated handlers, on essentially the same pricing basis as fully regulated handlers with respect to their fluid milk sales in the regulated marketing area.

Receipts of unpriced milk at a pool

plant, with limited exception, are assigned to the plant's surplus utilization. Such receipts include nonfluid products (e.g., nonfat dry milk) used for reconstitution of milk, milk from producer-handlers, and milk from unregulated supply plants that is designated for manufacturing. This assignment to surplus use recognizes that the value of such receipts is basically the surplus value. If such receipts exceed the plant's surplus use, the excess amount is assigned to the plant's Class I utilization. The regulated handler then must pay to the producer-settlement fund the difference between the Class I price and the surplus price on the amount assigned to Class I. This equalizes among pool plants the cost of milk used for fluid purposes.

If pool plant operators are short of regulated milk for fluid use, they may receive unpriced milk from an unregulated supply plant and have it assigned to their utilization pro rata with their receipts of regulated milk. To help equalize the pricing among pool plants of the amount assigned to Class I, the handler must pay to the producer-settlement fund the difference between the Class I price and the order's blend price.

Different accounting rules apply for regulated, or priced, milk moving from one Federal order market to another.

Packaged milk may be moved between Federal order markets on routes, or through interplant transfers, without any additional order obligation. In the case of interplant transfers, the packaged milk is assigned to Class I milk at the receiving plant.

Bulk milk received in one regulated market from another may be assigned to the surplus class if both

handlers agree. If both handlers do not agree on surplus classification, a percentage of such receipts, equal to the higher of the receiving market's average surplus utilization or the receiving handler's surplus utilization, is allocated to the receiving handler's surplus use to the extent such use is available. The remainder of such receipts is assigned to the handler's Class I utilization. This classification of other source receipts is passed back to the shipping market where the milk is priced. No further obligation applies under either order to the milk.

This allocation procedure for bulk milk results in local producer milk and milk from another regulated market sharing on a comparable basis in the receiving market's Class I and surplus utilization. However, if the receiving handler has a lower percentage of his milk in Class I than does the market, then the other source milk shares in the receiving market's Class I utilization only to this lesser extent. This discourages the uneconomic importation of milk.

### **Seasonal Pricing Plans**

Because the normal pattern of milk production results in a greater supply during the spring and early summer than during the remainder of the year, various plans of seasonal pricing have been used to encourage the production of milk on a more even basis. An incentive for a more uniform pattern of milk production may be provided in Federal milk orders by either "Louisville" (takeout-payback) plans or base-excess plans.

Louisville plans provide a specified amount of money be withheld in the flush-production season from the proceeds due producers. The money is placed in a special account and is then paid to producers in the short-supply season according to their

deliveries in that period. Under this plan, the funds withheld do not belong to particular producers, and any producer on the market during the payback period is eligible to share in the funds. The plan is most effective, of course, when producers remain on the market on a continuing basis.

The base-excess plan is a seasonal pricing plan which relates the payment more directly to the individual producer's seasonal pattern of deliveries. Under such a plan, producers establish a base equal to the average daily quantity of milk they deliver during the short-production season. During the following flush-production season, they are then paid the base price for quantities of milk delivered, up to the amount of their base, and a lower price for any additional milk delivered. The total payments for base and excess milk equal the total payments which handlers are required to pay for the milk at the class prices.

### **Class I Base Plan**

Class I base plans are designed to encourage dairy farmers supplying a market to tailor their milk marketings to the Class I needs of that market. Each producer is assigned a base which is a share of the market's Class I sales. The producer is paid a higher price for deliveries within that base and the surplus price for deliveries in excess of it.

Class I base plans provide that a producer's base will be based on deliveries of milk during a base-forming period of 1 to 3 years and will be automatically updated each year. Producers may reduce their marketings down to their base allocations without adversely affecting the future base size. Provisions are also made for new producers to

receive a base after 90 days on the market and for the alleviation of hardship and inequity among producers. Class I bases may be transferred on such terms and conditions prescribed in the order by the Secretary of Agriculture.

A separate referendum must be held on Class I base plans, and bloc voting by cooperatives is not permitted. If a Class I base plan is not approved by producers, it does not affect the status of the other provisions of an order.

The authority to include Class I base plans in Federal milk marketing orders was initially provided by the Food and Agriculture Act of 1965. It was revised and extended by the Agricultural Act of 1970 and again extended until December 31, 1981, by the Food and Agriculture Act of 1977. Class I base plans in effect prior to that date are authorized to continue in effect through December 31, 1984.

### **Advertising and Promotion**

A 1971 amendment to the Agricultural Marketing Agreement Act of 1937 provided the statutory authority for producers to develop advertising and promotion programs under Federal milk orders. The authority specifically provides for establishing nonbrand advertising, research, education, and promotional programs designed to improve or promote the domestic marketing and consumption of milk and its products. A separate referendum must be held to include an advertising and promotion program in an order. If such a program is disapproved by producers, the other provisions of the order are not affected in any way.

An advertising and promotion program is financed by deductions

on all producer milk. The deduction rate per hundredweight (45 kg.) of milk is specified in the order. For those producers who have a mandatory checkoff for advertising and marketing research under a state law, the order provides for a suitable adjustment or credit so that a producer does not have to pay to both programs. The Federal order also provides that any producer may request and obtain a refund of the monies deducted under the program relative to his marketings.

The collected funds are paid to an agency composed of producers and producer representatives that is responsible for developing programs to spend the funds. The composition of the board is specified in the order, with one representative usually provided for each specified percentage of participating producers. The order sets certain limitations on the expenditure of funds, and all programs and projects must be submitted to the Secretary of Agriculture for review and approval before they are undertaken.

# Administration of Federal Milk Orders

## Program Administration

Specific duties and responsibilities for the order program are delegated to the director of the dairy division by the Administrator of the Agricultural Marketing Service. The director has final authority to take action necessary or appropriate in the administration of milk marketing orders approved by the Secretary in accordance with the provisions of the Agricultural Marketing Agreement Act of 1937. Such action includes supervising the operations and activities of market administrators.

Each milk order is administered by a market administrator who is appointed by the Secretary of Agriculture. The powers and duties of the market administrator are prescribed in each order. The basic power given to (vested in) the market administrator is that of administering the order in accordance with its terms and provisions. In order to do so, the market administrator must make day-to-day decisions regarding the application of the order provisions to various circumstances.

Other powers of a market administrator include making rules and regulations to carry out the terms and provisions of the order, and receiving, investigating, and reporting complaints of violations to the Secretary.

The duties performed by a market administrator include those necessary to administer the terms and provisions of the order. These include a monthly computation and public announcement of class and uniform prices and associated butterfat differentials. The administrator verifies handler's reports and payments by inspecting the records of the handler. Another duty is to furnish to regulated handlers a

monthly statement of their accounts with the market administrator. The market administrator also prepares and disseminates statistics and other information on the market's supply and utilization of milk and milk prices.

The administrator employs a staff of auditors, and laboratory, clerical and data processing personnel to assist in administering the order. The cost of operating each order is assessed against regulated handlers in proportion to the volume of milk handled. A fund known as the administrative assessment fund is established under each order for this purpose. A separate fund known as the marketing service fund is also provided in most orders. This fund covers the cost of providing market information and for the verification of weights, samples, and butterfat tests of milk received from producers for whom such services are not being provided by a cooperative. This assessment is levied on the producers receiving the service.

One of the most important functions of the market administrator is the examination of books and records maintained by handlers to determine whether payments are made according to the terms of the milk order. Handlers are required to submit monthly reports showing their receipts and utilization of milk and payments to producers. Although the staff employed on specific duties varies from market to market, auditors make up 30 to 50 percent of all employees in most markets.

The audit program for verification of payments for milk combines a check of physical units and financial transactions. The comparison of intake and output of physical units and the customary balance of financial receipts and expenditures complement each other in the audit sys-

tem. The emphasis attached to physical and financial checks varies with the type of handling operation to be verified.

The auditor verifies by making comparisons of goods handled and financial records. Payments to producers and to other handlers are checked. Sales records are checked to support the reported disposition. Besides an investigation of the specific accounts which deal with purchases and sales that have a direct relation to milk handling operations, the complete audit includes an examination of other financial accounts to determine whether any account not labeled "milk" may have actually been used to record milk purchases or sales.

The complete financial check is usually interfused with the audit of production records. In the audit program, it is also customary to rely on a physical check of the handler's product operations as a means of verifying the total plant receipts and output. In this check of physical units, the receipts of milk are checked through the plant's production operations and balanced with the total recorded disposition.

The extent and type of the audit is adapted to the market and the handler in accordance with the terms of the orders and the records customarily kept.

The supervision of market administrators' operations and activities is carried out by the director of the dairy division by formal instructions, and through close working relationships between each administrator's office and the order operation, order enforcement, program analysis, market information, and cooperative qualification branches.

The director of the dairy division has

issued an instruction manual covering various aspects of the administration of milk orders. In addition, market administrators are required to report from time to time on special phases of their activities, such as auditing techniques or methods of testing the accuracy of weights and butterfat tests, so that these activities can be reviewed and evaluated.

The expenditure of funds by market administrators, both for administrative purposes and for marketing services to producers, is supervised by the director of the dairy division. Market administrators are required to submit for approval an annual budget of income and expenditures prior to the beginning of each calendar year. USDA's Office of the Inspector General audits the books and records of market administrators to determine if funds have been used in accordance with the approved budget and applicable instructions.

The responsibility for recommending the terms and provisions of milk orders and describing their intent and purpose is delegated to the director of the dairy division. When a market administrator, handler, or any other person has any questions concerning the application of a specific order provision, that person may request a ruling from the director. A handler who disagrees with an interpretation of an order provision may institute more formal procedures for review as outlined in a preceding section (Administrative and Legal Recourse).

### **Cooperative Qualification**

The Secretary of Agriculture has given the dairy division the responsibility for qualifying cooperatives under milk orders. Dairy cooperative associations marketing their members' milk under Federal

orders are entitled to certain benefits under the orders. These benefits include the rights and privileges to:

- bloc vote its members in referenda on proposed orders or amended orders;
- blend the net proceeds from sales of milk;
- provide its producers with market information and verify weights, samples, and butterfat tests of members' milk instead of having such services provided to its member-producers by the market administrator for a fee; and
- utilize special order provisions for cooperative associations in payment for milk or in the diversion of milk.

The basic standard provided in the Agricultural Marketing Agreement Act as to what constitutes a cooperative is that the association must be organized and operate in such a manner as to conform to the criteria contained in the Capper-Volstead Act. The Capper-Volstead Act was passed by Congress in 1922 to grant farmers who joined together to market their farm products a limited exemption from the anti-trust laws. The Capper-Volstead Act made it clear that farmers associated together, in stock as well as non-stock associations, could, without legal constraint because of the form of their association, collectively prepare for marketing and market their agricultural products.

The determination by the dairy division as to whether a cooperative qualifies for rights and privileges under a milk order is made only after a request by the cooperative. The division must take into consideration conditions that are specifically set forth in the Capper-Volstead Act in reaching a determination of whether or not a cooperative association is entitled to rights and privileges under milk orders. These conditions are:

1. It must be an association of agri-

cultural producers.

2. It must be engaged in marketing milk.
3. It must be operated for the mutual benefit of its members.
4. Its operations must be controlled by its members.
5. The value of its nonmember business must be less than the value of its member business.

The dairy division requires a cooperative desiring qualification to submit an application. These forms can be obtained on request from the dairy division. The application information and other data concerning the organization and operation of the association received from other sources are reviewed and investigated by the dairy division.

Once an association has established its eligibility, it is a "cooperative association" under the Federal order program and remains so as long as it continues to meet the prescribed standards. There is an ongoing as well as a formal annual review of the eligibility status of each qualified cooperative conducted by the dairy division to assure that rights and privileges are accorded only to entitled cooperatives.

### **Milk Market Information**

Another important function of the dairy division and market administrators is providing market information on supplies, sales and prices of milk to producers and handlers.

To assure the proper payment for milk under the orders, handlers are required to file reports showing the receipts of milk and butterfat from each source, and the quantities utilized in various forms such as fluid milk products, cottage cheese, butter, etc. Market administrators' offices collect marketing data from regulated handlers who account for

over 80 percent of the Grade A milk marketings and close to 70 percent of the total milk marketings in the country. From these handler reports, data are compiled and totaled for each market, and for all markets under the program. Since Federal milk order statistics are developed from records from all handlers and for all milk priced under Federal orders, rather than from sample data, such statistics provide reliable market information. Reported data are also subject to audit.

The statistical data collected under the Federal milk order program are an important segment of the information needed to administer the orders. These data are compiled and released for the use of persons who are interested in comprehensive information on milk supplies, utilization, and sales as well as prices established under the various milk orders. This information is helpful in current buying and selling decisions, in future planning, and to basic research undertakings by Government and others. The statistical information collected under the milk order program is probably the most comprehensive body of marketing information available on any agricultural commodity.

Federal order statistics and related price information are disseminated regularly through written reports issued weekly, monthly, and annually. Monthly and annual reports entitled "Federal Milk Order Market Statistics" may be obtained by writing to the Market Information Branch, Dairy Division, AMS, U.S. Department of Agriculture, Washington, D.C. 20250.

The dairy industry is a dynamic industry which has been characterized over the past 30 years by major changes in every segment of the industry. Major structural changes in milk production, farm milk assembly, processing, and distribution have been brought about by technical innovations and economic pressures to increase efficiencies.

The Federal order program has shown a remarkable ability to adapt itself to economic and technological changes which have occurred in the industry. Part of the ability can be ascribed to the considerable responsibility placed on the industry and other interested parties to propose and support changes at public hearings. The procedures under which milk orders are developed and amended are such that the impact of new marketing methods or other developments in the market can be publicly appraised. Public discussion and the exchange of views regarding marketing problems and their relation to the order program contribute to the solution of such problems. The complete and accurate information about supplies and sales of milk which is available in Federal order markets furnishes the material for better marketing decisions. These procedures have made the program responsive to the changing needs of the milk industry.

Milk orders have facilitated and accommodated innovations and efficiencies in production, handling and distribution. Nearly all of the structural changes in the industry have required substantial capital investments to achieve economies of scale. As a result, operating units at the farm, processing and distribution levels have become fewer in number and larger in size. As buyers and sellers have become larger, the milk marketing system has broadened and has become regional or even

national in scope.

Major structural marketing changes in the milk industry to which milk orders have adapted include the following:

- The number of commercial dairy farms has declined by more than 50 percent in the past quarter century. There are now about 170,000 compared to 400,000 in the mid-1950's. The decline in farms continues while herd size increases. Small herds with 1-19 cows have been disappearing rapidly. Dairy farms with 50 or more cows, although representing less than 20 percent of the farms, are producing more than 50 percent of the milk supply.

- Since the early 1950's, the number of milk processors has declined from some 8,500 to less than 1,200.

- There has been a complete conversion in fluid milk markets from can deliveries to bulk tank deliveries, and such conversion has been substantial in manufacturing milk markets.

- More than 80 percent of the total milk supply is now Grade A and the conversion to one grade of milk is continuing. This development is resulting in a single industry where the fluid and manufacturing segments are closely coordinated rather than the two separate industries which existed not too many years ago.

- There has been a tremendous expansion of both supply and distribution areas resulting from the erosion of restrictive health regulations and advances in refrigeration, transportation, and milk packaging. Many small receiving and distributing plants have been replaced by a larger ones which collect and

distribute milk over much broader areas.

- Large regional cooperatives have developed with membership among producers in several markets. Cooperatives now market more than 75 percent of the total milk marketed in the U.S. compared to about half in the 1950's. They have been major processors of manufactured dairy products for some time and continue to grow in this area. Cooperatives also are becoming more involved in the distribution of fluid milk.

- Retail sales have shifted from home delivery to chain stores. This has been accompanied by handlers increasingly processing, packaging, and delivering milk to stores only 4 or 5 days a week, leaving 2 or 3 days of raw milk production to seek outlets in other than fluid product markets.

- Many chain stores, in an attempt to capture some of the processing profits and to gain better management over their supply of milk, have vertically integrated backwards into the processing of fluid milk products.

Many of these dramatic changes would not have occurred with so little disruption had it not been for the orderliness and stability provided by the classification and pricing concepts which are basic to Federal milk orders. Moreover, the specific provisions covering classification and pricing in individual orders, as well as other provisions, have been amended when necessary to adapt to the changing needs of the milk industry. The net effect of changes in the milk order program over the past quarter century has been a shift from market orders geared to local conditions to a system of orders geared to regional and national conditions. Wider use of regional and national hearings has been made to

adopt these changes. Some of the changes include the following:

- Milk orders have been merged and expanded in response to widening areas of procurement and distribution.

- Uniform product classification provisions were adopted in more than one-half of the orders in recognition of the growing interrelationship of one market with another.

- A number of actions have been taken to provide a more stable price alignment among orders. The Minnesota-Wisconsin manufacturing grade milk price series was adopted to price milk for manufacturing use in Federal order markets. Later, this same price series became the basic formula price for determining the Class I price in all orders. Also, individual market supply-demand adjusters and Class I differentials which varied seasonally were eliminated.

- Substantially uniform provisions with respect to interhandler transfers and compensatory payments have been included in all orders. These changes facilitate the movement of milk between markets.

### **The Changing Nature of Federal Order Prices**

Over the years, the focus and nature of Federal milk order prices have changed. During the first 25 years of the program, Class I prices, as well as other class prices, and indeed entire orders, were tailored to the production and marketing conditions of the local marketing areas. There was little movement of milk between areas at that time and prices were viewed in terms of the appropriate level for a particular area. It was common in the earlier years to have

Class I price hearings for individual markets to correct a local pricing problem. The independence of markets during that period made it easier to deal with local changes in supply and demand. The matter of intermarket price alignment was secondary.

In the 1960's, however, it became evident that a more closely coordinated system of Class I prices was needed. Advances in transportation and refrigeration facilitated the movement of milk between markets and, thus, markets began to lose many of their local characteristics. The ability of a handler to obtain his supply of milk from sources outside the traditional milkshed made it necessary to give more weight to the cost of alternative milk supplies in establishing the Class I price level for a market. The increased mobility of milk made national supply-demand conditions an important factor in the supply-demand conditions of local markets.

To provide coordination in pricing among the markets, the Minnesota-Wisconsin (M-W) milk price series was adopted in the 1960's as the basic mover of Class I prices in all Federal order markets. Many orders, however, maintained local supply-demand adjusters in their Class I pricing formula. These supply-demand adjusters raised prices as supplies decreased relative to sales, and decreased prices when supplies increased relative to sales. The local supply-demand adjusters were phased out in the mid-1960's when it became evident that the local nature of markets could not be maintained and that a greater degree of intermarket price alignment was necessary.

Today, Class I prices under the orders are seldom changed on the basis of changes in local supply-

demand conditions in individual markets. Instead, Class I prices are viewed as a coordinated system of prices for the various markets where in the major factor moving prices up or down is the national supply-demand situation. Changes in individual order prices usually are made only in the context of a system of prices for all markets. No significant changes in the overall level of Class I differentials have occurred through the hearing process since 1968.

Changes in the Class I price level under the orders depend on changes in the M-W price which are brought about by changes in various open-market forces and the price support program. The M-W price series reflects a price level determined by competitive conditions which are affected by supply and demand conditions throughout the dairy industry, and reflects actions taken under the dairy price support program.

Much of the current alignment of Class I prices among the various markets was established in the late 1960's. Class I prices in various markets, until about 1972, were closely aligned with the Chicago Class I price plus transportation. Since that time, milk transport costs have increased substantially, but inter-market differentials in the orders have remained unchanged. This means that order prices no longer cover the cost of moving milk out of the surplus-producing rest of the upper Midwest into other markets.

One reason that Class I differentials have not been increased to reflect additional transportation costs is that markets generally have remained adequately supplied at existing Class I price levels. When supplies have tightened, cooperatives have obtained over-order payments to

help cover the cost of importing needed supplies.

The Agricultural Marketing Agreement Act of 1937 authorizes the Secretary of Agriculture to establish minimum prices to be paid by handlers for milk used in each use classification. Prices established under Federal orders are minimum prices only and handlers may pay producers higher than minimum prices. Since the order price system reflects the national supply-demand situation for milk, cooperatives from time to time have stepped in and charged prices above order minimums when a local or regional situation differed from the national. Over-order prices also have been used in some markets to cover transportation charges not fully covered by order provisions and to cover costs to manufacturing plants that make milk available for fluid use. During periods of tight supply, over-order prices tend to increase as distance from the upper Midwest area increases, and thus tend to reflect more fully than order prices the cost of alternative supplies.

In recent years, cooperative associations have been performing many of the services that were performed by proprietary handlers in the past. Federal order prices do not provide specifically for additional services provided by cooperatives in selling milk to handlers. These services would include the procurement, assembling and reserve disposal functions, along with a number of other services such as quality control, payrolling, and standardization. These services cost cooperatives money and, if a cooperative is to return the Federal order blend price to producers, it must recover such costs. Cooperatives attempt to secure reimbursement through over-order charges.

At any given time, market prices for milk above Federal order minimum prices may be possible, or even desirable, since the market price may reflect economic and competitive conditions which are not incorporated into the order minimum price structure. Cooperatives have relied more upon over-order charges in recent years as a way of fine-tuning order prices promptly to changed conditions and supplementing the minimum prices established under the orders.

### **Relationship of the Federal Milk Order Program with the Dairy Price Support Program**

Under the Agricultural Marketing Agreement Act of 1937 which authorizes the milk order program and the Agricultural Act of 1949 which authorizes the dairy price support program, the Secretary of Agriculture is charged with establishing a structure of prices which will assure an adequate but not excessive supply of milk. Congress gave the Secretary of Agriculture further direction for establishing milk prices when it passed the Agriculture and Consumer Protection Act of 1973, which amended both the 1937 Act and the 1949 Act. It requires that milk prices be established at a level that will assure a sufficient quantity of pure and wholesome milk to meet current needs, and to assure a level of farm income adequate to maintain productive capacity sufficient to meet anticipated future needs. The total supply of milk depends on the prices received by producers of Grade A and manufacturing grade milk, their costs of producing milk, alternative income-producing possibilities on and off the farm and their future expectations. On the other hand, the demand for milk and dairy products depends on their prices, consumer income, the availability and price of substitutes,

changes in consumer tastes and preferences, and changes in population. More than any time in the past, achieving a balance between supply and demand requires establishing a structure of prices which recognizes the sum total of forces affecting the national supply and demand for milk for fluid and manufacturing uses.

At one time milk orders were looked upon only as a means of achieving adequate supplies of milk for fluid use. The prime focus of the price support program was on prices of manufacturing grade milk and bufferfat, although such price did undergird the general level of all milk prices. Today, because the Nation's milk supply is predominately Grade A and because of the growing interrelatedness of the fluid and manufacturing segments of the industry, the milk order and price support programs are viewed in combination as devices by which the Government attempts to achieve an adequate supply of milk for both fluid and manufacturing uses.

Present programs put primary responsibility on price supports as the Governmental means for adjusting price levels to encourage changes in milk supplies. This is because milk prices under Federal milk orders are based on the average price paid for manufacturing grade milk in Minnesota and Wisconsin, which reflects the impact of all supply-demand factors operating in the dairy economy, including the dairy price support program.

The level of the Class I prices under Federal milk orders affects the blend price, which in turn influences how much milk is produced by dairy farmers delivering milk to Federal order markets. The level of the Class I prices also influences the consumption of milk in fluid form,

which impacts on the volume of milk available for manufacturing. Since over two-thirds of the milk marketed is covered by Federal milk orders, the level of the Class I prices affects the national supply-demand balance and the volume of removals under the dairy price support program.

In turn, changes in the dairy support price level, when market prices are at support, are reflected directly in the M-W price and in the level of all order prices. Thus, changes in the support price impact on the production and consumption of milk in all Federal order markets.

Using the M-W price series as a mover of class prices in all Federal order markets provides the program coordination between the Federal orders and the dairy price supports that is necessary to assure consistency in the Secretary of Agriculture's policies in establishing milk prices under the two programs. Since minimum class prices are tied to the M-W price, they will not keep rising and creating unneeded supplies of milk when USDA is trying to discourage milk production through actions under the dairy support program.

Because of the interrelatedness of milk orders and the price support programs, it has been increasingly necessary to look upon the combined effects of milk orders and price support levels in appraising the appropriateness of the overall level of Class I prices and price support levels. When supplies of milk relative to demand are in reasonably good balance, the combined effect of the two programs is prices consistent with the goal of long-run equilibrium. In combination, Class I price levels and price support levels are about right.

The Federal milk order program also

assists in carrying out the Congressional objective of supporting the price of all milk to assure an adequate supply. The classification and pricing concepts of orders are a means of securing adequate supplies of milk for fluid use, thus complementing the price support program. This reduces somewhat the reliance that the Secretary of Agriculture must place on the price support program to generate milk prices high enough to achieve adequate supplies of milk.

### **Trend Toward a Single Grade of Milk**

Eighty-three percent of the milk supply marketed is now Grade A while in 1950, only about 61 percent of the milk marketed was Grade A. The increase in the volume of Grade A marketed is even more significant than these percentages would imply, however, since the volume of whole milk marketed has increased substantially. Grade A marketings to plants and dealers in 1978 were around 97 billion pounds, more than double the estimated 45 billion pounds of Grade A whole milk marketed to plants and dealers in 1950. Only about half of this Grade A milk was used in fluid products in 1978, with the remaining volume used in manufactured products, particularly the so-called "soft" manufactured products such as cottage cheese, ice cream and yogurt. Two-thirds of the manufactured products produced in 1978 were made from Grade A milk.

There are a number of factors which have influenced the conversion from Grade B to Grade A milk production. Among these factors are:

- Classified pricing and market-wide pooling have resulted in higher prices to Grade A producers and

have encouraged conversion to the production of Grade A milk.

- Standards for Grade B are being raised and are closer to Grade A requirements in many of those states where the majority of the Grade B milk is concentrated. This makes it easier to convert to Grade A.

- The handling of manufacturing milk in milk cans is disappearing rapidly. Many manufacturing plants now have converted entirely to bulk tank handling systems and will no longer receive can milk from producers. With the can milk market disappearing in most areas, a producer so situated must convert to bulk tank handling or leave the business. After the bulk tank is purchased, the additional steps and investment necessary to convert to Grade A production are usually minor.

- Manufacturing plants which supply milk to fluid plants are required to segregate their receipts of Grade A and Grade B milk. To economize, many plants are eliminating these costly duplicate receiving and handling facilities and are receiving only Grade A milk. Producers delivering to these plants thus must convert to Grade A production or seek another market for their Grade B production.

- In spite of improvements in the quality of Grade B milk, health authorities are increasingly requiring that ice cream and cottage cheese be made from Grade A milk or Grade A milk products. Fortification of fluid milk products must be with Grade A nonfat dry milk. In addition, strong evidence exists that the quality of dairy products is higher and more consistent when made from Grade A milk. Plant managers recognize this and thus have encouraged their producers to improve the quality of their milk.

- Pooling provisions under Federal orders have made it fairly easy for plants to qualify as a pool plant, thus making it easy for producers who have converted to Grade A to share in the proceeds from the fluid market.

The continuing improvement in the quality of the milk supply and the trend toward a single grade of milk have changed the way the milk supply and the dairy industry is perceived. The dairy industry for many years was thought of as having two separate segments—a fluid segment and a manufacturing segment. The existence of two separate grades of milk—fluid grade or Grade A and manufacturing grade—was part of the reason for this distinction. The distinction was further emphasized by setting up two major Government programs—fluid milk orders designed primarily to assist Grade A producers who serve fluid milk markets and the dairy price support program aimed more at the manufacturing segment of the industry, but still undergirding the general level of all milk prices as well.

The steady trend towards a single grade of milk plus the increasing use of Grade A milk in manufactured products have made earlier distinctions of two separate supplies of milk no longer realistic. Increasingly, Grade A milk is being looked upon by the industry as the basic milk supply needed for fluid use and for use in soft manufactured dairy products. In addition, there are indications that processors of top-quality manufactured products are showing increasing preference for Grade A milk, thereby assuring themselves a supply of consistently high-quality milk.

Many persons in the dairy industry feel that the trend toward Grade A production will continue and that in

not too many more years we will have essentially a single grade of milk in this country.

If this occurs, significant changes will be required in the price support and milk order programs. As manufacturing grade milk disappears, so will the M-W manufacturing grade milk price, which is used in pricing milk in all Federal milk orders. This means new methods for calculating class prices under milk orders would be required. Also, the procedure of supporting the price of all milk by putting a floor under the manufacturing grade milk price would have to be changed. The price support objective would likely have to be expressed in terms of an "all milk" price rather than a manufacturing grade milk price.

## Measures of Growth in Federal Milk Order Markets, 1947-79

Year	Number of markets <sup>1</sup>	Popula- tion of Federal milk areas <sup>2</sup>	Number of handlers	Number of producers <sup>3</sup>	Pro- ducer deliveries	Producer deliveries used in Class I	Percent- age of producer deliveries used in Class I
	<i>Number</i>	<i>1,000</i>	<i>Number</i>	<i>Number</i>	<i>Million pounds</i>		<i>Percent</i>
1947	29	*	991	135,830	14,980	9,808	65.5
1948	30	*	963	136,363	15,020	9,852	65.6
1949	33	*	966	142,995	17,049	10,104	59.3
1950	39	*	1,101	156,584	18,660	11,000	58.9
1951	44	39,891	1,343	172,327	20,117	12,718	63.2
1952	49	41,185	1,352	176,752	22,998	14,672	63.8
1953	49	41,506	1,308	183,479	25,896	15,436	59.6
1954	53	43,266	1,333	186,127	27,140	16,172	59.6
1955	63	46,963	1,483	188,611	28,948	18,032	62.3
1956	68	48,575	1,486	183,830	31,380	19,615	62.5
1957	68	57,297	1,889	182,551	33,455	21,339	63.8
1958	74	60,717	1,962	186,155	36,356	23,309	64.1
1959	77	67,720	2,197	187,576	40,149	26,250	65.4
1960	80	88,818	2,259	189,816	44,812	28,758	64.2
1961	81	93,727	2,314	192,947	48,803	29,859	61.2
1962	83	97,353	2,258	186,468	51,648	31,606	61.2
1963	82	100,083	2,144	176,477	52,860	32,964	62.4
1964	77	99,333	2,010	167,503	54,447	33,965	62.4
1965	73	102,351	1,891	158,077	54,444	34,561	63.5
1966	71	98,307	1,724	145,964	53,012	34,805	65.7
1967	74	103,566	1,650	140,657	53,761	34,412	64.0
1968	67	117,013	1,637	141,623	56,444	36,490	64.6
1969	67	122,319	1,628	144,275	61,026	39,219	64.3
1970	62	125,721	1,588	143,411	65,104	40,063	61.5
1971	62	142,934	1,529	141,347	67,872	40,268	59.3
1972	62	142,934	1,487	136,881	68,719	40,938	59.6
1973	61	141,472	1,355	131,565	66,229	40,519	61.2
1974	61	141,546	1,312	126,805	67,778	39,293	58.0
1975	56	144,467	1,315	123,855	69,249	40,106	57.9
1976	50	149,493	1,305	122,675	74,586	40,985	54.9
1977	47	150,093**	1,260	122,755	77,947	41,125	52.8
1978	47	150,131**	1,189	119,326	78,091	41,143	52.7
1979	47	150,131	1,129	116,444	79,437	41,008	51.6

\*Data not available. \*\*Revised.

<sup>1</sup>End of year. (Date on which pricing provisions became effective.)

<sup>2</sup>End of year. 1951-59, 1960-70, and 1971-79 according to 1950, 1960, and 1970 U.S. census, respectively.

<sup>3</sup>Average for year.

<sup>5</sup>Prices are simple averages for 1947-61 and weighted averages for 1962-79.

Year	Prices at 3.5 Percent butterfat content <sup>4</sup>		Receipts as percentage of milk sold to plants and dealers		Daily deliveries per producer	Gross value at blend price adjusted for butterfat content	
	Class I	Blend	Fluid grade	All milk		Per producer	All producers
	<i>Dol. per 100 lb.</i>		<i>Percent</i>		<i>Pounds</i>	<i>Dollars</i>	<i>1,000 dol.</i>
1947	4.65	4.34	*	21	302	5,024	682,407
1948	5.29	4.97	*	22	301	5,713	779,079
1949	4.67	4.03	*	23	327	5,019	717,748
1950	4.51	3.93	41	25	326	4,914	769,442
1951	5.13	4.59	44	27	320	5,605	965,900
1952	5.37	4.85	46	30	356	6,598	1,166,246
1953	4.91	4.31	49	31	387	6,355	1,166,015
1954	4.62	4.01	49	31	399	6,098	1,135,019
1955	4.67	4.08	51	32	420	6,510	1,227,815
1956	4.90	4.24	51	33	466	7,534	1,384,955
1957	4.87	4.51	53	34	502	8,147	1,487,153
1958	4.72	4.40	56	36	535	8,500	1,582,310
1959	4.79	4.43	60	40	586	9,466	1,775,583
1960	4.88	4.47	64	43	648	10,482	1,989,615
1961	4.91	4.45	67	45	704	11,131	2,147,656
1962	4.80	4.14	70	47	761	11,854	2,210,330
1963	4.78	4.15	70	48	821	12,814	2,261,437
1964	4.87	4.23	70	48	888	14,174	2,374,137
1965	4.93	4.31	70	48	944	15,300	2,418,526
1966	5.55	4.95	70	48	994	18,526	2,630,908
1967	5.85	5.17	71	49	1,056	20,321	2,858,351
1968	6.23	5.53	74	52	1,089	22,561	3,195,087
1969	6.50	5.74	77	56	1,164	24,892	3,591,293
1970	6.74	5.95	79	59	1,244	27,636	3,963,311
1971	6.90	6.08	80	60	1,316	29,893	4,225,340
1972	7.10	6.31	78	60	1,372	32,439	4,440,288
1973	8.03	7.31	78	60	1,386	37,461	4,928,514
1974	9.35	8.36	78	61	1,464	45,376	5,753,852
1975	9.36	8.64	79	63	1,532	49,233	6,097,768
1976	10.70	9.75	80	65	1,661	60,277	7,394,486
1977	10.59	9.69	80	66	1,740	62,692	7,695,764
1978	11.40	10.57	80	67	1,793	70,528	8,415,787
1979	12.88	11.97	80	66	1,870	83,193	9,687,317









